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TESTIMONY OF AARP IN OPPOSITION TO HB 5184

Before the Michigan House Energy and Technology Committee

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I. INTRODUCTION

Mr. Chairman and Members of the committee, thank you for allowing us the opportunity to testify on House Bill 5184. My name is Melissa Seifert and I am the Associate State Director for Government Affairs for AARP Michigan. AARP is a nonprofit, nonpartisan 501(c)(4) social welfare organization with a membership of more than 37 million, including 1.4 million members in Michigan. AARP opposes this legislation because we believe HB 5184 jeopardizes the affordability and reliability of home energy. With me today I have Janee Briesemeister, Senior Legislative Representative from AARP's national Government Affairs team.

Mr. Chairman and Members, thank for the opportunity to testify here today. My name is Janee Briesemeister, Senior Legislative Representative in AARP Government Affairs, State Advocacy and Strategy Integration. I work with all of AARP's state offices on issues relating to advocacy for affordable home energy. Affordable home energy is a goal for AARP, and we have found that the consumers have not experienced the benefits they were promised with deregulated retail energy markets. AARP state offices in states with deregulated retail energy markets have been actively engaged in advocacy efforts to reform those markets to mitigate the negative consequences. AARP does not support any further deregulation of state retail energy markets, and we urge Michigan not to adopt further deregulation.

AARP advocates on policy issues that matter the most to people age 50 and over, and their families. A substantial percentage of AARP's members live on a fixed or limited income. A major priority for AARP is to protect consumers from unaffordable expenses for essential energy services that may endanger their health and financial security.

II. SUMMARY

AARP opposes HB 5184. Deregulation or "restructuring" (as it is sometimes referred) of retail energy markets has been a bad deal for residential consumers. They have faced higher prices, threats to reliability and numerous problems relating to aggressive marketing practices.

- Retail energy market competition has failed to deliver on promises of lowering prices for residential customers.
    - Electricity is not like other commodities. It is an essential service, and seniors devote a higher share of their average spending to utilities than do younger households.
    - According to a recent analysis, on average prices in deregulated states are 3 cents per kWh above rates in regulated states.
    - Data shows the offers by third party suppliers have generally resulted in higher prices for residential customers compared to the distribution utility's default service.
    - Worse, the recent "polar vortex" resulted in alarming spikes in residential utility bills, some doubling, tripling, or even more.
    - Retail marketers largely rely on short term purchases in the wholesale markets, which are vulnerable to extreme price swings. There have also been numerous examples of market manipulation by generators, resulting in price increases for consumers. A regulated utility is better able to manage its generation and fuel portfolio and mitigate such extremes in price swings.
    - Costs will also increase to consumers, because deregulation itself comes with costs. The expense to implement retail competition will be significant, including an unknown level of stranded costs, as well as costs to implement adequate licensing, billing, and market oversight of retail suppliers in their interactions with distribution utilities and consumers.
    - It is not clear whether a "standard" or default service is required, and there is no guidance to ensure that this service is procured through a portfolio of contracts designed to assure price stability and lowest cost. The bill eliminates the current law's requirement that generation supply be provided at a "reasonable cost." Without this requirement, standard offer could be based on the volatile, short term wholesale market, subjecting consumers to extreme price swings.

- Reliability of generation supply is at risk with deregulation.
    - Once utility capacity is sold off, there is no guarantee that a deregulated wholesale market will supply adequate generation, in part because the tighter the supply, the higher the prices generators can charge.
    - FERC and the courts have prevented states such as New Jersey and Maryland from taking actions to ensure sufficient generating capacity would be available for their consumers.
    - Texas, which is not under FERC jurisdiction, continues to debate how to prevent blackouts as generation reserves are shrinking and blackouts threaten.

- Retail competition has resulted in marketplace nightmares for consumers.
    - The typical deceptive and unfair contract terms that are prevalent and generate complaints in other states include:
        - teaser rates
        - variable rates with no means of determining the pricing mechanism
        - door to door and telemarketing sales, much of which is aimed at lower income customers and customers who may not speak English or otherwise understand the details of these transactions
        - supplier misrepresentation of identity
        - additional fees and charges that are hidden in fine print
        - hefty early termination fees
        - poor or nonexistent customer service

As one of our members recently testified in Connecticut:

> *I believe I am a savvy consumer. I look for good deals and know a scam when I see one. As a 30 year customer of UI [United Illuminating], I saw a chance to save some money and switched to a retail supplier. For a few months I saw savings and was quite pleased. However, I lost that entire savings and more because, as it turned out, I had signed up for a variable rate that, after a very short introductory period, increased significantly. The variable rate was 35% higher than the standard offer. I learned a lesson about shopping in the retail market that left a bad taste in my mouth.*

- Other states are continually working to fix their broken retail energy markets.
    - Once a state implements deregulation, it's difficult to undo, no matter the severity of the rate increases, the abuses in sales and marketing, or the dysfunction as a whole.
    - There are investigations, hearings and proposed legislation in several states to address the latest price spikes.
    - States must react to each crisis, passing reforms that provide a temporary fix until the next abuse or market dysfunction develops.

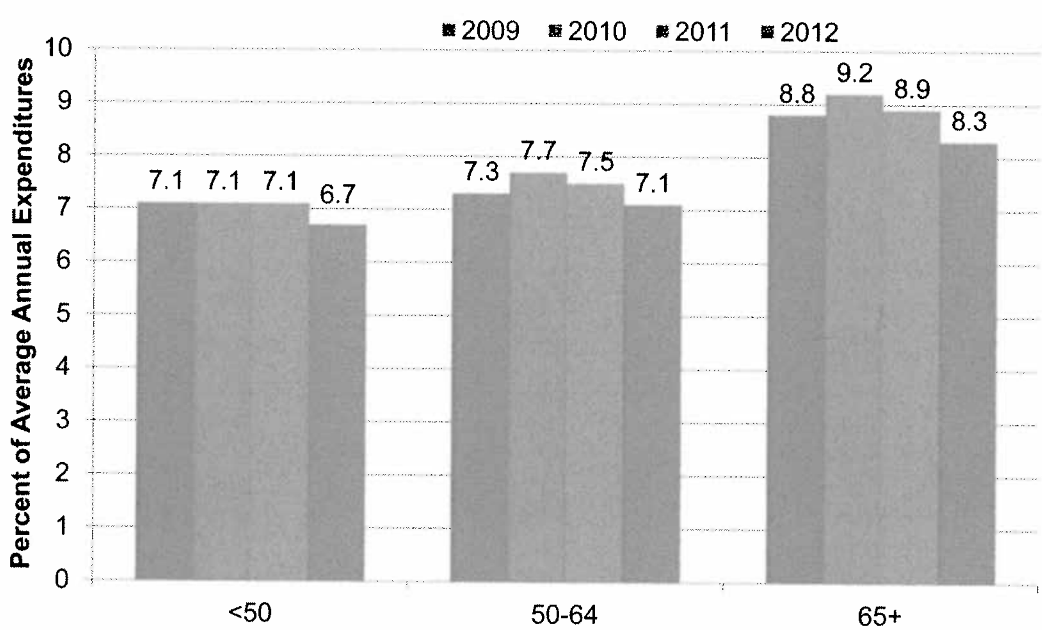
AARP agrees with the goal of making energy more affordable in Michigan. However, we strongly disagree that lifting the 10% cap will achieve that goal, especially not for residential consumers.

III. ELECTRICITY IS AN ESSENTIAL SERVICE

Electric service is essential to all residential customers, and the affordability of this service for low and fixed income customers whose energy burden is high in relationship to their income is crucial. Affordable electricity is essential for lighting, refrigeration, and cooling, a characteristic not shared by most other consumer goods and services, for which substitutes exist. Unaffordable electricity in Michigan's often severe winter climate has dire consequences for residential customer health and safety.

Low income families, and households with medically frail and very old or very young members, are particularly vulnerable to excessive prices. It is well documented that many families face the choice between cooling and eating or purchasing vital medical supplies. Older Americans who cannot afford basic energy services are particularly vulnerable to health impacts due to insufficient heating or cooling. AARP's analysis of federal data shows that utility expenditures are a higher percentage of average annual expenditures for older consumers.

Figure 1: Utility Expenditures Comprise a Higher Percentage of Average Annual Expenditures for Consumers Age 50+



Source: AARP Public Policy Institute analysis of 2009, 2010, 2011, and 2012 Consumer Expenditure Surveys.

IV. RETAIL ENERGY MARKET COMPETITION HAS NOT DELIVERED ON ITS PROMISES TO LOWER PRICES FOR RESIDENTIAL CUSTOMERS

Competition for goods and services is a bedrock principle for the U.S. economy and generally results in benefits for consumers. However, the electricity market is not the same as other consumer goods and services. Electricity cannot be stored. Electricity is priced in the wholesale market based on the expectation that it will be immediately available to meet the load requirements of customers, large and small, in every hour of every day. In most restructuring states the third party suppliers are typically middle-men that buy on the wholesale market and seek to make a profit by selling generation supply to retail customers. **There is no way to ensure lower prices for Michigan's consumers if this bill is enacted, and all evidence from other states shows that higher rates are the more likely outcome.**

Analyses that purport to show benefits of retail competition in other states lack facts relevant to residential customers, or do not show a complete picture. As an example, a recent study from Illinois purports to show savings from deregulation, but fails to point out that the savings are based on significant government intervention to control costs, including a $1 billion refund resulting from the Attorney General's legal action against market manipulation; the establishment of the Illinois Power Agency to procure power for consumers at reasonable and stable rates; and the widespread implementation of municipal aggregation, where local governments seek to procure power in the market at the lowest cost. Meanwhile, seeking further government intervention, Exelon has signaled it will ask the Illinois Legislature to force Illinois ratepayers to subsidize its money-losing nuclear plants. Should that nuclear bail-out occur, any potential savings that could go to consumers due to lower generation prices will be wiped out as Illinois ratepayers bail out a company in a competitive business. How is that a good deal for consumers?

Expert analyses show a less than rosy picture for consumers under deregulation.[1] According to a recent analysis, prices in "deregulated" states are, on average, 3 cents per kWh above rates in regulated states. This gap is slightly higher than the gap of 2.8 cents per kWh that existed among these same states in 1997, the onset of the restructuring era.[2] States such as New York, New Jersey and

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[1] The COMPETE Coalition maintains that the move to restructuring has resulted in savings in electricity costs to consumers, but their publications are noticeably lacking in facts that are relevant to residential customers, and their membership is primarily composed of commercial and industrial customers. See, e.g., Comments of the COMPETE Coalition in the New York Commission's Proceeding on Motion of the Commission to Assess Certain Aspects of the Residential and Small Non-Residential Retail Energy markets in New York State, Case 12-M-0476 (January 25, 2013). Contrast these statements with an analysis of Kenneth Rose, *State Retail Electricity markets: How are They Performing So Far?*, Electricity Policy.com, http://electricitypolicy.com/articles/4455-stateretailelectricitymarkets (available by subscription). Dr. Rose concludes that consumer benefits have not yet appeared or been documented, particularly for residential customers.

[2] See, American Public Power Association (APPA), *Retail Electric Rates in Deregulated and Regulated States: 2012 Update*, available at: http://www.publicpower.org/files/PDFs/RKW%5FFinal%5F%2D%5F2012%5Fupdate.pdf

Connecticut had the highest electricity prices in the continental U.S. prior to restructuring, and they still do.

Often Texas is cited as an example of a successful deregulated retail market, but studies paint the same picture of higher prices for residential consumers. A recent study found:

> *All told, Texans living in deregulated areas would have saved more than $22 billion dollars in lower residential electricity bills since 2002 had they paid the same average prices as Texans living outside deregulation. The lost savings amounts to more than $4,500 for a typical household since 2002.*[3]

Furthermore, as substantiated by the examples presented in the attachment, the rate options and contract offers by third party suppliers have, in many cases, generally resulted in higher prices for residential customers compared to the distribution utility's default service. The recent "polar vortex" resulted in alarming spikes in residential utility bills, some doubling or even tripling, because retail marketers rely on short term purchases in the wholesale markets, which are vulnerable to extreme price swings. A regulated utility is better able to manage its generation and fuel portfolio and mitigate such extremes in price swings.

Further, there have been numerous instances of market manipulation in the regional wholesale markets, resulting in high prices to consumers. Unfortunately, even after a finding of fault or settlement, consumers have only rarely gotten any refunds after overpaying due to market manipulation.

Costs will also increase to consumers because deregulation itself comes with costs. The expense to implement retail competition will be significant, including an unknown level of stranded costs, as well as costs to implement adequate licensing, billing, and market oversight of retail suppliers in their interactions with distribution utilities and consumers.

All of the evidence shows that consumers can expect to experience higher prices under deregulation.

V. RELIABILITY OF GENERATION IS AT RISK WITH DEREGULATION

Another claim made is that deregulation will not affect resource adequacy and in fact, may incentivize new construction of generation at lower cost. The facts on the ground show that is again a false assumption. House Bill 5184 follows the path of most deregulated states by requiring utilities to sell or spin off their generation fleet. This will move generation to the wholesale markets, under

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[3] http://tcaptx.com/wp-content/uploads/2013/12/TCP-793-ElectricityPricesInTX-A-1.8.pdf

jurisdiction of the Federal Energy Regulatory Commission. These regional wholesale markets have been characterized by price volatility and growing concern that in some, there will be insufficient resources to meet demand. There is no guarantee that a deregulated wholesale market will supply adequate generation, in part because the tighter the supply, the higher the prices generators can charge.

Maryland, New Jersey and Connecticut each took action to ensure sufficient generating capacity would be available for their consumers by allowing local utilities to enter into contracts that support the development of new generation. However, the Maryland and New Jersey actions were challenged at FERC as violating the market structure established by FERC. Thus far, those challenges have been upheld by and in the courts, thus preventing states from taking steps to ensure generation reliability for consumers when the wholesale market does not.

Texas, which is not under FERC jurisdiction, continues to debate how to prevent blackouts as generation reserves are shrinking and blackouts threaten. [4] The market alone has provided "insufficient incentives" to induce generators to construct sufficient capacity to meet the state's needs. [5]

VI. RETAIL COMPETITION HAS RESULTED IN MARKETPLACE NIGHTMARES FOR CONSUMERS, INCLUDING VARIABLE RATE CONTRACTS, MISLEADING SALES PRACTICES AND SLAMMING

Shopping for electricity has not been a good experience for residential customers. Some larger commercial and industrial entities might be able to negotiate contracts with wholesale or retail suppliers that would provide an advantage compared to utility prices today, but residential and small commercial customers do not have this option. Rather, they are presented with "take it or leave it" preprinted contracts with prices that will, in most cases, be higher than those that the utility can provide through either their own generation or with competitive bids obtained in the wholesale market. Even when prices are lower, that lower price is often a teaser rate, which rises dramatically and with little notice.

All of the deregulated states except Texas have a standard offer or default service to provide service to customers at a reasonable cost. Yet, even then customers who find they got a bad deal in the market cannot switch due to high early termination fees.

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[4] http://app1.kuhf.org/articles/1386612493-Freezing-Weather-Nearly-Sends-Texas-Into-Rolling-Blackouts.html

[5] http://www.powermag.com/texas-and-the-capacity-market-debate/

AARP regularly hears stories from its members about aggressive sales techniques, inaccurate portrayal of the standard offer, misleading advertising, cancellation fees, variable rates with no caps and inadequate customer service.

- Consumers are told repeatedly that they will receive "lower bills" or "savings" in marketing materials from alternative suppliers, but while the initial teaser rate may be slightly below the current Standard Offer price, the contract typically relies on variable prices after the initial term that are significantly higher than the Standard Offer price.

- Variable rates are disclosed as "based on wholesale market conditions" and do not reflect any publicly available index or formula that a consumer can access to determine the degree of variability in the prices based on historical conditions or even predict their next monthly bill. A typical example is the following disclosure from Blue Pilot Energy:

  Price per Kilowatt Hour. You have a variable rate plan with a starting price set at 7.5 cents per kWh. This initial rate will be effective for at least the first ninety (90) days of service. Thereafter, your price may vary on a month-to-month basis. This price includes Generation Charges, but excludes applicable state and local Sales Taxes and the Delivery Charges from your LDU. At any time after ninety (90) days of service, but not more frequently than monthly, Blue Pilot may increase or decrease your rate based on several factors, including changes in wholesale energy market prices in the ISO New England Markets. Your variable rate will be based upon ISO-NE wholesale market conditions. Please log on to www.bluepilotenergy.com or call Customer Service at 877-513-0246 for additional information and updates.[6]

- Another typical marketing disclosure is that offered by Starion Energy in which customers are told in large and bold print that SAVINGS are promoted, and a price is listed slightly below the current Standard offer, but in tiny print at the bottom of the brochure is stated, "Starion Energy's rate is variable, therefore is subject to change in response to market conditions."[7]

- Door to door and telemarketing sales agents are typically independent contractors that are paid by the licensed supplier based on a successful sale, a sales arrangement that often results in untrained agents, an incentive for misrepresentation, and even in some rare cases, criminal conduct.

VII. DETAILED COMMENTS ON HB 5184

House Bill 5184 would make radical changes in the current statutes applicable to Michigan's electric market structure. Specifically:

1. It is not clear whether a "standard" or default service is required, and there is no guidance to ensure that this service is procured through a portfolio of

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[6] Provided in response to OCC Interrogatory #37, PURA Docket No. 13-07-18.
[7] Provided in response to OCC Interrogatory, PURA Docket No. 13-07-18.

contracts designed to assure price stability and lowest cost. The bill eliminates the current law's requirement that generation supply be provided at a "reasonable cost." Without this requirement, standard offer could be based on the volatile, short term wholesale market, subjecting consumers to extreme price swings.

2. The bill would require that utilities divest or transfer generation assets and purchased power contracts. This directive is likely to result in higher prices as all power will be procured through the wholesale markets. Recovery of stranded costs by utilities will also increase utility costs for consumers.

3. The bill's proposed municipal aggregation authority would eliminate affirmative customer consent and would allow aggregation only with a negative option or opt out. Some have called that essentially a "government slamming" program that would transfer customers to alternative suppliers under prices and terms and conditions that are unknown at this time.

4. There is only very general language regarding essential consumer protections regarding the marketing and sales conduct of alternative suppliers. There are no specific directives or minimum standards of conduct set forth in this legislation.

5. The bill does not provide any additional protections or additional bill payment assistance to low income customers.

VIII. OTHER STATES ARE CONTINUALLY WORKING TO FIX THE BROKEN RETAIL MARKET

The term "you can't put the toothpaste back in the tube" is often used with regard to attempts to reform the deregulated retail energy markets. That's because once done, its difficult to undo, no matter the severity of the rate increases, the abuses in sales and marketing, or the dysfunction of the market as a whole. A few states have stopped or reversed course, but most continually react to each crisis, with most passing reforms that provide a temporary fix until the next abuse or dysfunction develops.

AARP has been involved in these debates across the country, with the goal of mitigating harm to consumers. For example, AARP called for the New York Public Service Commission to investigate consumer complaints about marketing abuses and high rates, and the commission recently issued an Order[8] that calls for

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[8] New York Public Service Commission, Proceeding on Motion of the Commission to Assess Certain Aspects of the Residential and Small Non-residential Retail Energy Markets in New York State, CASE 12-M-0476, ORDER TAKING ACTIONS TO IMPROVE THE RESIDENTIAL AND SMALL NONRESIDENTIAL RETAIL ACCESS MARKETS (Issued and Effective February 25, 2014).

significant reforms to its market for residential customers, including a mandate that suppliers not charge low income customers more than the default or standard service price, that utilities must provide a bill calculator that allows customers to compare their historical bills paid to suppliers with the default or standard offer, and a prohibition on allowing distribution utilities (as allowed in this bill) to disconnect service to customers for an amount that would exceed what the customer would have paid for default or standard service. This latter policy is in direct response to the findings that significantly higher prices were being paid by the vast majority of residential and low income customers served by alternative suppliers compared to the utility's default or standard offer service.

In addition, both Pennsylvania and Connecticut have recently opened new investigations into hundreds of complaints received from customers in their states that documented extremely high prices—many in the range of 20 cents per kWh—charged by suppliers under variable rate contracts that included provisions that allow a monthly price change based on "market conditions." At the same time, other states struggle with how to ensure adequate generation capacity to prevent blackouts.

IX. CONCLUSION

AARP agrees with the goal of making energy more affordable in Michigan. However, we strongly disagree that lifting the 10% cap will achieve that goal, especially not for residential consumers. AARP urges the Michigan Legislature to reject HB 5184.

Thank you again for the opportunity to testify today. Please feel free to contact Melissa Seifert at (517) 267-8934 or mseifert@aarp.org if you have questions or require further information.